« Return to article

Print this

The Straits Times
www.straitstimes.com
Published on Sep 11, 2014

Singaporeans' puzzling behaviour at age 55

ASK: NUS ECONOMISTS

Q: What do Singaporeans do with their Central Provident Fund savings withdrawn at age 55?

A: Many countries rely on pension savings to meet individuals' retirement needs. A key question that arises is whether individuals should be allowed easy access to pension savings.

Easier access may make pension savings more flexible and attractive, generating more savings and higher retirement income. But there is concern that access to one's pension savings can result in excessive present consumption at the expense of future retirement security.

Despite the importance of this issue for policy formulation, the evidence remains limited on the reasons for pension saving withdrawal and the usage of these funds.

For example, in Singapore, the Prime Minister in his National Day Rally speech raised concerns about the viability of Central Provident Fund (CPF) savings and the wisdom of letting people access their CPF funds at the age of 55. There has been a lot of discussion on this topic since, and some have argued that letting people withdraw the money is unwise as it may lead to excessive current consumption at the cost of lower levels of savings for the older years.

In a recent research paper, we attempt to shed more light on this issue.

Since Singapore allows individuals to cash out a fraction of their CPF at age 55, we wanted to find out:

First, do consumers actually withdraw their CPF when they have the option of doing so at age 55? Second, how does the option to withdraw CPF savings at age 55 affect the consumption and savings decisions of these consumers? Third, what motivates the withdrawal decision of these consumers? Do they make decisions due to credit constraints and demand for financial flexibility?

Today, CPF members reaching 55 can withdraw at least $5000, as well as CPF balances in excess of the Minimum Sum of $155,000.

Aggregate statistics from the CPF board show that close to SG$3 billion of CPF funds are withdrawn each year, which amount to about 1 per cent of the 2011 Gross Domestic Product in Singapore.

The average withdrawal was SG$11,000 per person, almost triple the average monthly salary in the population.

We wanted to examine CPF withdrawal and subsequent consumption behaviour.

To do so, we used a unique panel dataset of monthly consumer financial transactions from a large financial institution in Singapore. We then examined the response of bank account balances (which serves as a proxy for the withdrawal amount), credit card spending and debit card spending to reaching the withdrawal age.

The data that we use spans from April 2010 to March 2012. During this period, Singaporeans were allowed to withdraw between 10 and 30 per cent of their CPF cash balances on their 55th birthday, regardless of whether they had met the minimum sum.

We find that, on average, as individuals became eligible to cash out a fraction of their retirement savings, their bank balances rose by about SG$15,000 (approximately 2.5 times that of average monthly income in our sample) one month after turning 55.

Strikingly, despite the large withdrawal, cumulative credit and debit card spending rose by only about $600 twelve months after turning 55.

Most of this spending was driven by an increase in debit card spending and increased spending for poorer consumers. Richer consumers, on the other hand, did not change their spending patterns appreciably in response to the increase in disposable income.

Overall, bank account balances decline by about one third after 12 months, with the balance remaining significantly higher (SG$10,000) than before the member turned 55, even at the end of our sample period.

Which individuals had swollen bank balances upon turning 55 - who might be those who had withdrawn their CPF?

We find that consumers' demographics, especially those related to financial literacy and sophistication are important determinants of the withdrawal decision.

Consumers with more banking experience or access to financial advisors through a priority bank account were significantly less likely to withdraw their CPF savings.

Being eligible to withdraw CPF funds when they turn 55 does not appear to have a large effect on the consumption patterns of the average consumer, suggesting most people do not intend to consume (much of) their withdrawn funds.

On the other hand, the withdrawal decisions of these near-retirement consumers are also fairly puzzling - on average, consumers neither spend, nor do they invest the withdrawn money in more productive savings vehicles.

The average Singaporean consumer appears to be willing to forego an estimated 4 per cent interest rate by choosing to leave their withdrawn balances in a low-interest bearing savings account rather than in their Retirement Account.

But one caveat of our analysis is that we do not observe consumers' financial behaviour beyond the one year horizon - one possibility is that consumers may begin to invest their CPF withdrawals in higher-yielding interest accounts after one year.

Caveats aside, our findings suggest that consumer financial literacy and sophistication are important factors driving withdrawal decisions. This suggests that early access to pension savings may lead individuals to make sub-optimal savings decisions.

But there is little support in our findings for the major concern that consumers will overspend their withdrawn savings and fritter away all their retirement savings when given the option to access their pension savings.

Sumit Agarwal is Low Tuck Kwong Professor of finance and real estate, and research director at the Centre for Asset Management Research and Investments.

Jessica Pan is assistant professor of economics; and Wenlan Qian assistant professor of finance. All three are from the National University of Singapore.

This is a monthly series by the NUS Economics Department. Each month, a panel will address a topical issue. If you have a burning question on economics, write in to stopinion@sph.com.sg with “Ask NUS” in the subject field.

stopinion@sph.com.sg